Economics

Economic Indicator — July 17, 2024

Housing Starts Turn Up in June

Gain Owed to Volatile Multifamily Segment, Single Family Continues to Pull Back

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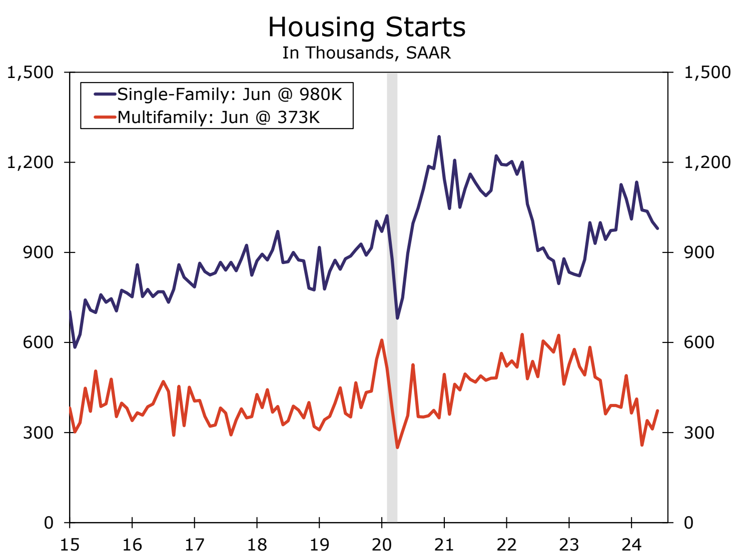
Summary

Multifamily Jump Overshadows Single-Family Slump

High interest rates are beginning to weigh more heavily on residential construction. Total housing starts rose 3.0% to a 1.35-million-unit pace during June. However, the consensus-beating upturn occurred largely as a result of a surge in multifamily starts, which are highly volatile on a monthly basis. Despite June's gain, multifamily starts are still down sharply over the past year alongside softer apartment market fundamentals and tighter credit conditions.

Meanwhile, both single-family starts and permits once again pulled back during June. Builders now appear to be scaling back production alongside slowing new home sales and rising inventory levels. All told, the headwinds created by restrictive monetary policy appear to be intensifying for home builders. Financing their operations has become more expensive and demand appears to be waning as a result of elevated mortgage rates, increased supply in the resale market and cooling labor market conditions.

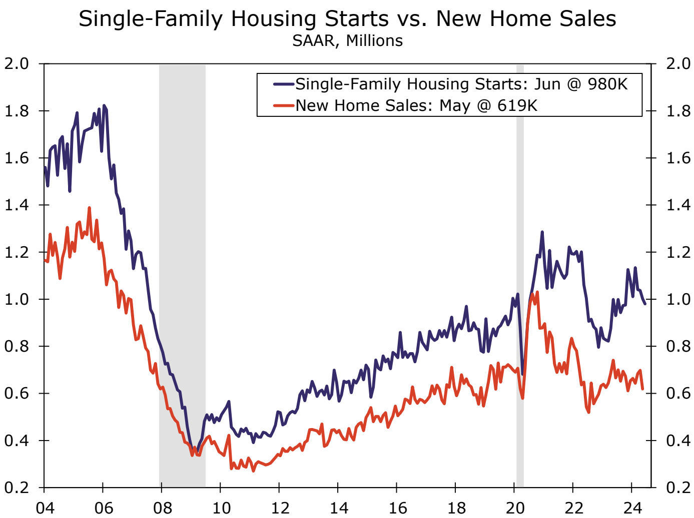
Against this backdrop, the NAHB Housing Market Index declined for the third consecutive month in July. Although rate cuts should eventually help enliven activity, the recent dip in single-family permits and dimming builder sentiment suggests residential construction will continue to lose momentum over the next several months.



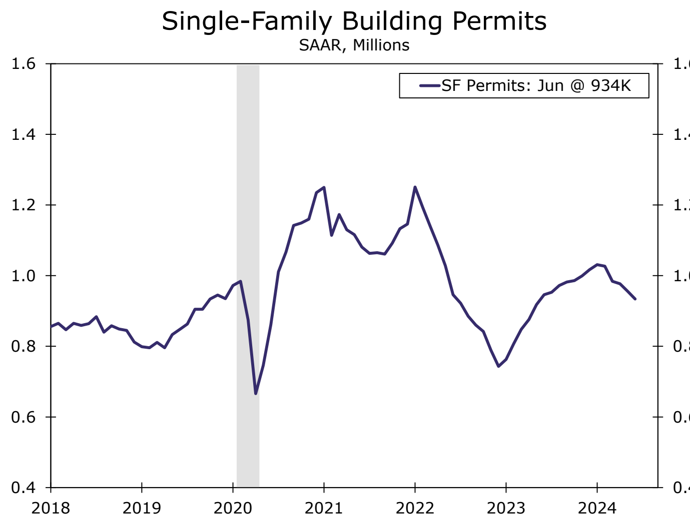
Source: U.S. Department of Commerce and Wells Fargo Economics

High Mortgage Rates Keep a Lid on Single-Family Building

- Persistently elevated mortgage rates amid a tighter stance of monetary policy have sapped builder confidence and reduced residential construction in recent months. The 30-year fixed mortgage rate has hovered around 7.0% for most of this year, averaging 6.9% in June.
- Single-family housing starts posted its fourth sequential decline in June, dipping 2.2% to a 980K-unit pace. This drop coincides with a five-month downdraft in single-family permits.
- At 934K, the pace of single-family housing permits in June retreated to its lowest level since May 2023.
- Although builders are leaning on incentives to improve affordability, weakening new home sales serve as evidence that high rates have push buyers back to the sidelines. The pace of new home sales in June registered its second lowest reading since October 2022.
- We expect single-family construction to improve on balance this year, but high mortgage rates will remain a substantial headwind. If our expectation for monetary policy easing comes to fruition this fall, however, lower mortgage rates should help to restore builder confidence and reinvigorate buyer demand.
- The NAHB Housing Market Index declined to 42 in July, the third straight monthly drop. Although sentiment regarding future sales notched a small improvement, present sales and buyer traffic both declined. To some extent, builders have been able to side-step higher interest rates by offering rate buy-downs, price discounts and other incentives. Slower new home sales and rising inventory levels indicate that those incentives are not as persuasive as they once were, with a cooling labor market now also a headwind.



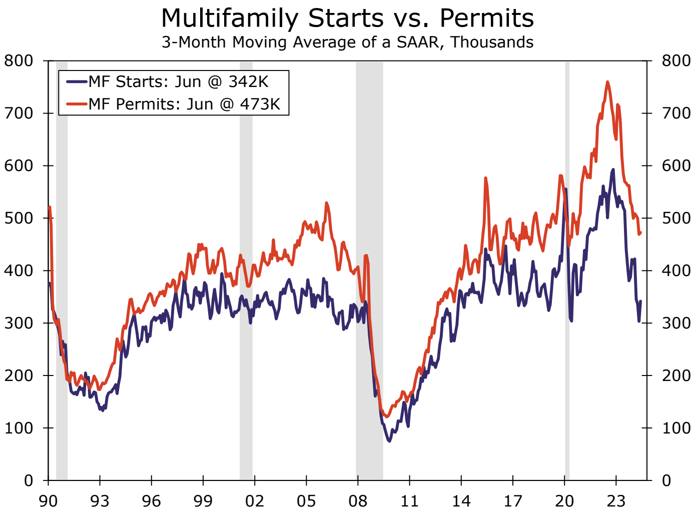
Source: U.S. Department of Commerce and Wells Fargo Economics



Source: U.S. Department of Commerce and Wells Fargo Economics

Surge in Multifamily Construction More Noise than Trend

- Multifamily starts improved notably in June, jumping 19.6% to a 373K-unit pace.
- Multifamily permits similarly leaped 15.6%, partially offsetting the prior three-month string of declines.
- That said, multifamily data is highly volatile and activity is still weakening through the monthly noise. Multifamily permits were down 22.9% on a year-to-date basis in June.
- Despite the bounce in activity over the month, we still expect the trend decline in new permits will set the stage for more modest multifamily construction in the years ahead.
- One factor contributing to a lower number of new multifamily projects is the robust pipeline of units already under construction. There were 895K units under construction in June, 126K off of the peak reached one year ago but still elevated far above historical norms. For context, there were an average of 621K apartments under construction per month in 2019.



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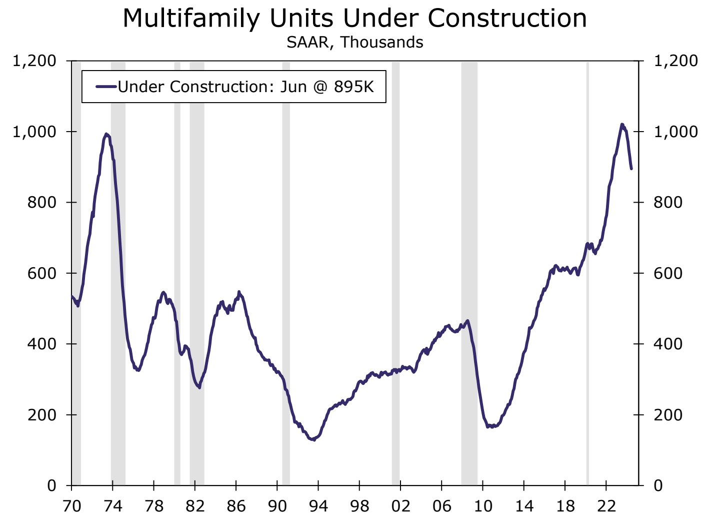

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